BRIEF IN SUPPORT OF PETITION FOR WRITS OF CERTIORARI.

OPINIONS BELOW.

A reference to the opinions below is set forth in the Petition at page 2 thereof.

JURISDICTION.

The grounds upon which the jurisdiction of this Court is imposed are set forth in the Petition at page 2 thereof.

STATEMENT OF THE CASE AND QUESTIONS INVOLVED.

The Petition contains a statement of the questions involved at page 2, and a statement of the case at page 3.

STATUTES INVOLVED.

The statutes involved are referred to in the Petition at page 3.

SPECIFICATION OF ERRORS TO BE URGED.

The errors which will be urged if the writs of certiorari are granted are that the Circuit Court of Appeals for the Third Circuit erred:—

1. In failing to apply the primary test of whether the trusts were enterprises for the transaction of business or were created and maintained as a medium for the carrying on of a business enterprise and sharing its gains before considering corporate resemblance.

2. In failing to hold that the purposes of the trusts were to hold and conserve the trust property with incidental powers.

3. In holding that the primary test is the similarity of the benefits enjoyed by virtue of the trust when compared with those afforded by the use of the corporate forms.

4. In holding that the presence of the five attributes afforded by corporate organization mentioned by this Court in *Morrissey v. Commissioner,* 296 U. S. 344, 359, were sufficient in themselves to classify the trusts as associations.

5. In holding that all five of said attributes were to be found in the two trusts.

6. In holding that the question at issue was whether the trusts were associations or "pure trusts", that is trusts of the traditional pattern, and that the trusts involved in these cases were associations because they did not resemble "traditional trusts".

7. In failing to construe the term "associations" in its literal and ordinary meaning and giving said term a strained construction not justified by the language used, other provisions of the Revenue Acts and the general scheme of taxation intended by Congress in the Revenue Acts.

8. In failing to hold that the investors were not associates.

9. In failing to hold that the trusts were taxable as trusts.

10. In holding that the trusts were associations and hence taxable as corporations.

11. In affirming the judgments of the District Court.

Argument.

We will first discuss rulings of the Commissioner and the opinions of the District and Circuit Courts. We will then expand our argument upon the first four reasons relied on for the allowance of writs of certiorari and will conclude our brief with an analysis of other Circuit Court cases relied on below and our concluding summary.

THE RULINGS OF THE COMMISSIONER AND THE DECISIONS OF THE DISTRICT AND CIRCUIT COURTS.

The Commissioner first ruled that one of the trusts administered by the petitioner was an association and then under date of May 18, 1936 reversed his ruling and held that the legal effect of the plan set forth in the trust was that each investor makes the trustee an agent without discretion and merely for the purpose of holding the naked legal title of the property of its principal. (R. 25)

The Commissioner under date of January 28, 1937 reversed himself again and held that thirteen trusts administered by the petitioner were associations. (R. 26) The basis for the reversal was that the trustee had the authority to substitute investments, that the trusts were investment trusts and that all investment trusts whether of the fixed or management type were taxable as associations under the regulations. On this latter point it is sufficient to point out that the Circuit Court of Appeals for the Eighth Circuit in *Commissioner v. Buckley*, 128 F. (2d) 124, disposed of an argument that all investment trusts were associations by stating that such a conclusion was not justified by the opinion of this Court in the *Morrissey* case, and that Congress itself has consistently recognized that an investment trust is not necessarily an association by imposing issuance and transfer taxes upon its shares "whether or not such investment trust * * * constitutes a corporation within the meaning of this title". (Internal Revenue Code Section 1802 (a) and prior Revenue Acts.)

The District Court (R. 30-61) rested its conclusion that the trusts were associations solely upon the ground that the power to substitute investments was management. It did not find that the trusts were joint business enterprises or that they had been created and maintained to provide a medium for the conduct of a business and sharing its gains. Its approach to the cases was superficial and in sharp contrast with its approach and well reasoned opinion in a case involving a fixed investment trust decided on the same day, *Pennsylvania Co. etc., Trustee v. United States,* 48 F. Supp. 969.

In its argument before the Circuit Court the respondent did not attempt to justify the decision of the District Court on the narrow grounds stated in its opinion. It advanced the argument that any trust which is not "a pure trust" must necessarily be a business trust, and relied upon the secondary test of the five features of the resemblance to corporate organization mentioned by this Court in the *Morrissey* case.

The Circuit Court substantially adopted the argument of the respondent. While it did not actually hold that any trust which is not a pure trust must be a business trust, this is the effect of its opinion. It stated that the issue involved was whether the trusts involved were pure trusts or associations. (R. 66) It held that the term "associations" as employed in the Revenue Acts embraces "business trusts", and that what Congress did not intend to embrace within the term "associations" were "pure trusts, that is, trusts of traditional pattern where property is conveyed by will, deed, or declaration to a trustee or is to be retained by the settlor on specified trusts for a certain term for the benefit of named or described persons." (R. 71) It erroneously held that "under the *Morrissey* case the test primarily is the similarity of the benefits and privileges enjoyed by virtue of the trust when compared with those afforded by the use of the corporate forms" (R. 72),

went on to list the five features which this Court mentioned in said case, held that when they are found in a trust they are "sufficient to characterize it as an association" (R. 72), and then erroneously held that all five features were to be found in the trusts here involved. (R. 73) It held that the power of substitution of the sponsoring companies was reposed in them for a business reason (R. 73) and that it was exercisable by the distributing companies according to their "business purposes and motives". (R. 74)

The Circuit Court further distinguished the trusts here involved from "traditional trusts" on the basis that the trustee's functions resemble those of a custodian, that in essence the investors were merely purchasers of the shares, and that each investor has the several right to exhaust the trust res while the trustee remains helpless. It overlooked that these facts are evidence that the trusts do not resemble corporations. The limited nature of the functions of the trustee negatives the element of centralized management, and the power of the investors severally to repossess their interest in the trust res is an element found in ordinary revocable trusts and negatives the concept of a continuing entity holding assets which is characteristic of a corporation. The Circuit Court concluded without justification that the trusts had not been formed for the purpose of holding and conserving property in the manner ordinarily afforded by a trust, and again confused the business activities of the distributing company, in whose profits the investors do not share, with the participation of the investors in the trusts. (R. 74) The only purpose assigned to the investors, which resembles a business purpose, is that they participate in the trust "in the hope of a return by way of dividends and of gain through the possible enhancement in the value of the trust shares". (R. 74) It is sufficient to say that such is the hope of every member of the investing public, that there is no evidence supporting this finding, and that this Court has held in *Higgins v. Commissioner*, 312 U. S. 212, that the investment activities an individual do not constitute doing business.

It is significant that the Circuit Court did not attempt to apply the primary test of the *Morrisey* case by first determining whether the trusts were formed and maintained for the purpose of entering into a business enterprise and sharing its gains. The decision of the Circuit Court thus raises several fundamental points. Shall the question be tested by the superficial test of resemblance to corporate organization, or shall the primary test be whether the trust is a business trust? Shall the term "associations" be given its ordinary and literal meaning or shall it be extended beyond the clear import of the language used? Shall any doubt be resolved in favor of the taxpayer, especially when a finding in favor of the government results in double taxation of the same income?

I. THE CIRCUIT COURT FAILED TO FOLLOW THE MORRISSEY CASE.

Prior to the *Morrissey* case the leading case in this Court was *Hecht v. Malley*, 265 U. S. 144. In that case it was held that Massachusetts business trusts were associations although formed under trust agreements rather than under statutes. Prior cases holding to the contrary were distinguished in view of changes in the Revenue Acts. This Court there held (p. 157) that "the word 'association' appears to be used in the Act in its ordinary meaning" and quoted the following definitions found in standard dictionaries, which were again quoted in the *Morrissey* case (p. 352); "a body of persons united without a charter, but upon the methods and forms used by incorporated bodies for the prosecution of some common enterprise"; "a body of persons organized for the prosecution of some purpose, without a charter, but having the general form and mode of procedure of a corporation"; "an organized but unchartered body analogous to but distinguished from a corporation".

In 1935 this Court decided the *Morrissey* case and also its companion cases, *Swanson v. Commissioner*, 296 U. S. 362; *Helvering v. Combs*, 296 U. S. 365; and *Helvering v.*

Coleman-Gilbert Associates, 296 U. S. 369. There was no doubt in each of these cases that the trusts under consideration were business trusts. The trusts in the *Morrissey*, *Swanson* and *Coleman-Gilbert Associates* cases were real estate trusts under which the trustees were empowered to develop and deal extensively in real estate. The Combs trust was formed for the purpose of developing an oil property. The point argued in the *Morrissey* case was that beneficiaries of the trust had no powers to control the policies of the trustees similar to the powers of stockholders of a corporation. This Court held that this one factor was not sufficient to classify the trust as a trust rather than as an association.

The opinion of this Court in the *Morrissey* case stated at considerable length the fundamental principles by which the question was to be determined. The primary test was whether the trusts had been created and maintained as "a joint enterprise", or "an enterprise for the transaction of business" (p. 356), or to provide "a medium for the conduct of a business and sharing its gains" as distinguished from an object "to hold and conserve particular property with incidental powers" (p. 357). "The nature and purpose of the co-operative undertaking will differentiate it from the ordinary trust." (p. 357). The importance of this primary test is emphasized by the fact that this Court used the same or similar language repeatedly in the course of its opinion.

The secondary test is resemblance to corporations (p. 357). This Court, of course, did not undertake in its opinion to point out all respects in which a business trust might resemble a corporation. It mentioned five features (p. 359) which have been referred to in subsequent lower court decisions. These five features are not primary tests of the fundamental question and were never intended to be so construed. They all may be found in a trust as well as in a corporation, and were merely enumerated as features which may be evidence of resemblance to corporate organization.

The only case on the question which this Court has since decided in *Lewis & Co. v. Commissioner,* 301 U. S. 385, which serves to demonstrate that the principles announced in the *Morrissey* case are not to be unduly extended.

There are a number of federal cases, decided since the *Morrissey* case, which approach the problem by first determining whether the trust is a business trust. If it is not, the secondary test of corporate resemblance is not controlling. The cases which involve trusts of securities are: four fixed investment trust cases; *Commissioner v. Chase National Bank,* 41 B. T. A. 430; 122 F. (2d) 540; *Commissioner v. Buckley,* 128 F. (2d) 124; *Pennsylvania Company, etc. v. United States,* 48 F. Supp. 969; *Pennsylvania Company, etc. v. United States,* 48 F. Supp. 972; a periodic payment plan trust case, *Equitable Trust Company v. Magruder,* 37 F. Supp. 711; and a case involving a trust set up by the Chrysler corporation for the benefit of its officers, *Estate of Frederick L. Alldis v. Commissioner,* 46 B. T. A. 1171. Among the cases involving other kinds of trusts are *Cleveland Trust Company v. Commissioner,* 115 F. (2d) 481 (certiorari denied, 312 U. S. 704), and *United States v. Davidson,* 115 F. (2d) 799.

Commissioner v. Chase National Bank, supra, is the leading case upon fixed investment trusts. A fixed investment trust contains a number of resemblances to corporate form. The so-called "depositor", which corresponds to the sponsoring company in our cases, has the power to require the trustee to sell the stock of any company, held in the trust, which in its opinion has become an undesirable investment. This power corresponds to the power of substitution in our cases. The Board of Tax Appeals held that the powers of the trustee were "purely ministerial", that the powers of the depositor were "among the usual powers of an ordinary trustee", that the trust provided no "medium for the conduct of a business and sharing its gains", and that "the trustee's operations could not be called 'an enterprise for the transaction of business' which the Supreme Court in *Morrissey v. Commissioner,* 296 U. S.

344, regarded as implicit in the statutory term 'associations' ". (41 B. T. A., at page 442) It did not consider corporate resemblances.

On appeal the Circuit Court for the Second Circuit held that "in determining the character of these trusts the powers and duties of the trustee should be added to those of the depositor in order to arrive at the full amount of permitted managerial activity and its object", that the power of elimination affected "the property held in trust only by weeding out whatever became unsound for investment", that the Board's finding that "the trust property was to be held for investment and not to be used as capital in the transaction of business for profit like a corporation organized for such purpose" was well supported, and that "this distinction is what makes the difference tax-wise" under the *Morrissey* case. (122 F. (2d) at page 543) No mention was made of corporate resemblances.

The *Chase National Bank* case was relied on by the Circuit Court for the Ninth Circuit in holding another fixed investment trust to be a trust for tax purposes. *Commissioner v. Buckley, supra.* It was also relied on in two fixed investment cases decided by the same District Court which decided our cases on the same day. In its opinions the District Court also examined corporate resemblances and found they were not controlling in view of the fundamental purposes of the trusts. *Pennsylvania Company etc. v. United States, supra* (two cases).

The *Magruder* case is important because it holds that a periodic payment plan trust is not an association in a well reasoned opinion and correctly applies the primary test. The Collector in that case filed an appeal to the Circuit Court of Appeals for the Fourth Circuit and thereafter withdrew his appeal.

The *Alldis* case, which has been appealed and has been argued before the United States Circuit Court for the Sixth Circuit, is important because the trust there under consideration granted to the Chrysler Corporation very consid-

erable powers of management. The Commissioner ruled that the trust was a trust and not an association and has consistently maintained that position both before the Board of Tax Appeals and the Circuit Court.

There is still another case as yet unreported which was set for argument before the Circuit Court of Appeals for the Tenth Circuit on January 17th, 1944: *Commissioner v. City National Bank and Trust Company, Trustee.* The opinion of the United States Tax Court may be found at ¶ 43, 131 of Prentice-Hall 1943-1944 Tax Court Memorandum Decisions Service. This case involves a trust which is a combination of a fixed investment trust and a periodic payment plan trust. The Tax Court held it to be a trust and not an association relying on the *Chase National Bank* and *Buckley* cases and on the *Magruder* case.

All of the Five Features of Resemblance to Corporate Organization Are Not Present in These Trusts.

The statement of the Circuit Court that all of the five features mentioned by this Court in the *Morrissey* case were present in the case of these trusts is erroneous. We will take them up in order but before doing so we point out that this Court stated in the *Morrissey* case that these five features were often to be found in trusts as well as corporations, so that it cannot be the law that a trust must be an association even if all five features are present.

1. A continuing entity as holder of legal title to the trust res. In a loose sense this feature is present, but in the sense that it is a feature usually found in a corporation we find two points of difference. In the first place, each individual investor may at any time terminate his certificate and possess himself of his share of the trust property or the proceeds thereof. A stockholder of a corporation has no such right and one of the advantages of the corporate organization is that the assets of the corporation cannot be disturbed by the individual stockholders. The action of the

stockholders voting as a group is required. In the second place, the trust res is allocated upon the books of the trustee to each individual investor in accordance with the number of shares which have actually been purchased with his own money. In this respect we have a separation and earmarking of the assets entirely foreign to corporate practices.

2. Centralized management through the trustee. The Circuit Court has found that the trustee's powers resembled those of a custodian. Its powers are ministerial and are limited by the terms of the trust agreements and certificates. There is certainly no central management lodged in the trustee in the sense that term is used in the *Morrissey* case, to wit, powers which are exercised "in much the same manner as directors". The powers of substitution are trust powers as we will demonstrate below.

3. Security from termination or interruption by reason of the death of owners of beneficial interest. This element is present but it is an element of a trust as well as a corporation. In the *Morrissey* case this Court stated that this element was more a distinction applicable to partnerships than a distinction between trusts and corporations (p. 359).

4. The facilitation of transfer of beneficial interests and the introduction of large numbers of participants without affecting the continuity of the enterprise. These elements are present, but again the distinction would seem to apply more to partnerships. Inasmuch as there may be thousands of participants in an employees' trust of a large corporation, and Congress taxes such trusts as trusts and not as associations, this element cannot have any great importance. See also *Swanson v. Commissioner, supra,* where this Court held that a limited number of participants did not affect the general question.

5. The limitations on the liability of the participants to the property embraced in the undertaking. There is no

basis whatsoever for the Circuit Court's finding that this feature was present in the two trusts involved. What this Court had in mind in the *Morrissey* case was a provision in the trust agreement that all persons dealing with the trustee were required to look for payment or indemnity only to the trust property (p. 347). There is no such provision in either of the trust agreements in these cases.

The Powers of Substitution Are Incidental Trust Powers.

The trustee of an ordinary trust under will or deed is granted the power to invest and reinvest the corpus of the trust. This is a fundamental trust power. Some trustees are limited in their powers of investments, others are given broad powers. A trust in which the trustee has broad powers would not be classed as an extraordinary trust.

This court held in *City Farmers Trust Company v. Helvering,* 313 U. S. 121, and *United States v. Pyne,* 313 U. S. 127, that the activities of a trustee in investing and reinvesting trust property did not constitute doing business, and that the expenses incurred in such activities were not deductible as business expenses for income tax purposes. The power to eliminate undesirable stocks from a fixed investment trust was held to be an investment power in *Commissioner v. Chase National Bank, supra,* at page 543; and it was recognized in *Cleveland Trust Company v. Commissioner, supra,* at page 484, that trustees ordinarily have the right to invest and reinvest and that this power does not convert a trust into an association.

The power of the sponsoring company to substitute under the Capital agreement is a very limited one. (Appendix p. 56.) In the first instance, substitution must be made in the shares of another fixed investment trust, if such shares are available; and the substituted shares must have underlying securities reasonably comparable to those underlying Independence Trust Shares. If such other shares are not available, or their purchase is impractical, the sponsoring company may, if it deems such investment

more beneficial to the investors, substitute receipts or certificates of interest issued by banks or trust companies, evidencing the deposit of underlying securities again reasonably comparable to the securities underlying Independence Trust Shares. The power of substitution under the Capital Agreement is therefore very limited in nature. It requires that an equivalent investment be furnished. It requires that the investment policy fixed by choosing Independence Trust Shares as the original investment be substantially carried on throughout the entire period of the trust. It will be further noted that the implication is that any substitution is to be made from the point of view of the best interests of the investors, and not to serve the business purposes of the sponsoring company.

In the Wellington Trust Agreement the power of substitution of the sponsoring company is broader (Appendix pp. 94-96), but again we find that the substitution in the first instance must be made in the shares of another investment trust, incorporated or unincorporated, having securities in its portfolio reasonably comparable with those in the portfolio of Wellington Fund, Inc., the original investment. If such shares are not available or the purchase of them is impractical, other shares may be substituted which in the opinion of the sponsoring company will supply the investors with shares of reasonable security and income producing characteristics. Here again, we have an implication that the best interest of the investors is to be taken into consideration. The standard to be applied requires like shares if possible, otherwise shares having investment characteristics of security and income rather than speculative characteristics designed to realize trading profits.

The power of the trustee to substitute can only be exercised when substitution is necessary in order to continue the operation of the plans. Under the Capital agreement the trustee can substitute only if the shares then purchaseable cease to be available for purchase and the company within sixty days after notice fails to provide other shares

(Appendix p. 59), or if the shares currently to be purchased can be purchased only at unreasonable prices (Appendix p. 59). In each case, however, the trustee must give thirty days' notice to each investor and it can substitute other shares only for those investors who give their consent in writing. In this respect the trustee's power is more limited than the power of an ordinary trustee who has authority to invest and reinvest without seeking the consent of the beneficiaries.

Under the Wellington Trust Agreement the trustee has the power to substitute only if the sponsoring company fails to furnish it with an adequate source from which it can purchase shares on demand at market value (Appendix p. 96), and again we find that its power to substitute is limited to those investors who give their approval in writing after thirty days' notice.

We submit that there was no basis for holding that the power of substitution in either trust was to be exercised for other than sound investment reasons, or that they were to be exercised except when "necessary" (Appendix p. 57 and p. 96) to the continuance of the trusts.

The fact that the powers of substitution have never been exercised in either of these trusts supports our contention that they are but incidental trust powers and are not powers of management. If the intention had been to invest and reinvest the trust property so as to take advantage of swings in the market and realize profits, the power of substitution would have been exercised again and again.

We are aware that in the *Helvering v. Coleman-Gilbert Associates, supra,* this Court held that a trust must be classified on the basis of what can be done under the trust agreement rather than what has been done. Every principle of law is applicable to the particular facts of the case. In the *Coleman-Gilbert* case the added powers which had not been exercised were very broad. The trustee was authorized to deal very extensively in real estate. The Circuit Court had held that the trust was a liquidating trust. This Court held

that it was not if these added powers were taken into consideration. The situation here is different. We have one single power which has some slight resemblance to central management. The question is whether it is a power of central management or merely an incidental trust power. The fact that it has never been exercised supports our argument that it was never intended to be more than an incidental trust power.

II. THE CIRCUIT COURT ERRONEOUSLY CONSTRUED THE INTENT OF CONGRESS.

This Court has held in a number of cases of which *United States v. Merriam,* 263 U. S. 179, is the leading case, that taxing statutes are not to be extended by implication beyond the clear import of the language used and that doubt as to the meaning of their words must be resolved against the government and in favor of the taxpayer. In a subsequent ruling the Commissioner held that dividends and distributions received for each investor upon his trust shares should be treated as distributed for federal tax purposes, whether remitted or invested in additional shares. The further rule of statutory construction announced by this Court in *Crocker v. Malley,* 249 U. S. 223, therefore also applies. In that case the late Justice Holmes held that a tax statute should not be construed to tax the same income twice unless the intent to do so is clearly expressed.

The respondent before the Circuit Court argued that any trust which is not a "pure trust" must be classified as an association. While the Circuit Court did not entirely adopt this argument, it construed the intent of Congress in such a manner as to substantially adopt the respondent's theory.

It stated that the question involved was "whether the trusts under consideration are pure trusts or associations taxable as corporations within the meaning of the Revenue Acts" (R. 66), and after holding it was certain that the term "associations" embraces "business trusts", it went

on to hold that what Congress did not intend to embrace within the term "associations" were "pure trusts, that is, trusts of the traditional pattern where property is conveyed by will, deed, or declaration to a trustee or is to be retained by the settlor on specific trusts for a certain term for the benefit of named or described persons". (R. 71) It then distinguished the trusts here involved from traditional trusts on the basis that the distributing companies were not settlors, that the investors were entitled to take down their interests in the trust at any time while the trustee remains helpless, and that the functions of the trustee amount to little more than a custodianship. It lost sight of the fact that each individual investor is a grantor of the trusts as far as his interest therein is concerned, and that its inference that the trusts have no grantors is unsound. It lost sight of the fact that the ministerial functions of the trustee negate the attribute of "central management through the trustee". It lost sight of the fact that the power of each investor to take down his interest in the trust at any time is a power which the grantor of any revocable trust may at any time exercise, and that in a revocable trust the trustee is equally helpless to maintain and preserve the trust estate intact if the grantor elects otherwise.

The fundamental question is what was the intent of Congress when it used the term "associations" in the statutes involved, applying well settled rules of construction of tax statutes? The intent of Congress must be construed so as to give the term "associations" its ordinary and literal meaning without extending the meaning beyond the clear import of the word used. The question at issue is not whether the trust is a pure trust or an association, but whether what is a trust in form and in substance must be construed to be an association resolving any doubt in favor of the taxpayer.

The general scheme of Congress under the various Revenue Acts has been to tax primarily income of individuals

and corporations. Partnerships are not taxed as separate entities. Their income is wholly taxed to the partners whether distributed or not. Trusts are not taxed upon distributed income and the income of some trusts, such as revocable trusts, are taxed entirely to the grantors. Income received by an agent is never taxed in his hands; it is taxed as the income of his principal. The sections of the Revenue Act and Internal Revenue Code which tax trusts do not disclose any intention to exclude "pure trusts", or "traditional trusts" from their operation. Under Section 161 of the Internal Revenue Code a tax is imposed upon the income "of any kind of property held in trust", the broadest kind of a clause. Section 165 of the Internal Revenue Code provides for the taxing of employees' trusts. The usual form of employees' trust is really an investment trust managed by a committee appointed by the employer for the benefit of employee beneficiaries. An employees' trust does not exactly fit the definition of a pure trust or a traditional trust contained in the Circuit Court's opinion.

The construction of the intent of Congress announced by the Circuit Court has led in these cases, and will inevitably lead in other cases, to the classification of trusts as associations on superficial and technical grounds. It bypasses the fundamental question of whether the trust is really an association in the ordinary and literal sense. The primary test adopted by this Court in the *Morrissey* case is the only sound test to apply in construing the intent of Congress. In order to justify the taxation of a trust as a corporation, it must really be an association; it must have been created for the purpose of conducting a business enterprise and sharing its gains.

The trusts involved in these cases are certainly ordinary trusts and they are traditional trusts within most of the elements contained in the Circuit Court's decision of that term. They are created by a trust agreement which is equivalent to a deed or declaration. The terms of the trust are specified with great particularity. The term of the

trusts with respect to each investor is as certain as is the term of any revocable trust. The beneficiaries are described persons, viz.: those persons who become beneficiaries by accepting certificates. The trusts are nonetheless trusts because the functions of the trustee are ministerial. Many trust instruments are so drawn and it cannot be said that such trusts are extraordinary as distinguished from ordinary trusts.

The two trusts involved in this case are as much like traditional trusts as the trusts involved in the cases cited above at page 22 of this brief. They are as much like traditional trusts as fixed investment trusts. They are very similar to the periodic payment plan trust in the *Magruder* case. In a great many respects they are more like traditional trusts than the trusts involved in the *Alldis* and *Cleveland Trust Company* cases. They are certainly as much like traditional trusts as liquidating trusts which often issue shares and often grant the trustee broad powers of management. The cases consistently hold that liquidating trusts are not associations so long as their purpose is liquidation, that broad powers in the trustee do not constitute central management and do not turn the activities of the trust into a business venture. (See *United States v. Davidson, supra.*)

III. THESE TRUSTS WERE CREATED AND HAVE BEEN MAINTAINED FOR THE PURPOSE OF CONSERVING AND HOLDING PROPERTY FOR THE SEVERAL BENEFIT OF THE INVESTORS.

There is no basis whatsoever for the conclusion of the Circuit Court that these trusts were not formed and maintained for the purpose of holding and conserving the trust property. The essence of a periodic payment plan is that as each investor makes his payments, the trustee, after making authorized deductions, purchases the designated shares for him, and that the shares purchased and accumulated from time to time shall be held in trust for long

periods of time unless the investor defaults or unless the investor determines to revoke the trust as far as he is concerned. The essence of a fully paid plan is that the shares purchased for the particular investor are to be held for him for a long period of time subject to his right of revocation.

Neither of the trust agreements disclose any purpose that the trustee shall engage in a business enterprise in the ordinary or literal sense. The very name "Capital Savings Plan" implies a purpose to accumulate an investment rather than to engage in business. The designation of the beneficiaries as "investors" in the Capital plan has a like implication. The same implication is contained in the first whereas clause of the Wellington Agreement (Appendix p. 87) which states that the purpose of the plan is "to provide the holders with a convenient means of a systematic and protected medium of saving and investment".

The Capital Trust Agreement evidences an intention that the trustee is to hold the shares purchased for each investor and for his account until he terminates his certificate. For instance, in Section 1 of Article II (Appendix pp. 45-46) it is provided that after the trustee has made the authorized deductions, the balance of the investor's payments "shall be invested by the Trustee for the account of the Investor". In Section 2 of the same Article (Appendix p. 46) it is stated that the trustee shall hold in its name as trustee the shares purchased by it "In Trust, for each of the several Investors in the respective series in the proportion to which they may be respectively entitled". In Section 3 of the same Article it is provided that the trustee shall collect all distributions on the shares and shall apply the same to the purchase of additional shares and "likewise hold the same in trust for the several Investors". In Section 7 of the same Article it is provided that after the trustee makes the authorized deductions from the single payment under the fully paid certificate, it shall apply the balance to the purchase of shares and "shall continue to hold the same for the benefit of

the Investor". In the certificates (Appendix p. 67 and p. 71) we find a provision reading that until the certificate shall have been terminated the shares "purchased for the account of the Investor shall be held by the Trustee, pursuant to the terms of the Trust Agreement".

There are other provisions in the trust agreements and the certificates which could be mentioned to illustrate the general purpose to hold and conserve the trust property, but we will not unduly extend this brief for that purpose. We submit that the principal object of the trusts is plain, viz: to hold the shares purchased for each investor for long periods of time until he elects to withdraw.

We submit that Congress never intended to tax trusts of this nature as corporations. They cannot be administered as corporations and we do not see how they could be organized as corporations. There are many fundamental differences and again in the interest of brevity we point out only the following.

1. The certificates do not resemble shares of stock (Appendix p. 65, p. 69 and p. 100). They take the form of a contract under which the individual investor agrees to make certain payments, authorizes certain deductions to be made therefrom and authorizes the balance to be invested in designated shares. They do not evidence a pro rata interest in a pool of assets. The investors do not buy shares in the trusts. They buy the share of an investment trust or investment company through the trustee.

2. The certificates are not transferable in the manner certificates of stock are transferable. They are contracts and are assignable in the manner ordinary contracts are assignable, that is with the consent of the parties and subject to the agreement of the assignee to become bound by the terms of the contract. (Appendix p. 84 and p. 88)

3. The trusts have no capital and surplus in the sense that a corporation has capital and surplus. The trustee keeps no capital and surplus accounts. (R. 9, 46)

4. Each investor has at any one time an interest in a definite part of the trust res, unlike the interest which a stockholder has in a corporation.

5. The investors have no voting rights with respect to the administration of the trusts. There is no provision for meetings of investors and no meetings have ever been held. (R. 9, 46)

6. Once the trustee accepts its trusteeship under a particular certificate it cannot resign or be removed unless there is a default under a periodic plan, except in a remote contingency in the case of the Wellington plan. (R. 68) In a corporation the stockholders have the right to elect a new board of directors.

7. There is no body which acts "in much the same manner as directors". (*Commissioner v. Morrissey, supra,* p. 359) The trustee's functions are ministerial and are prescribed by the trust agreements. The powers of substitution are trust investment powers.

8. There is no power to distribute profits which corresponds to the power of the board of directors of a corporation to declare dividends. The income received is not the income or profits of a common enterprise. The income received upon the shares held for each investor belongs to him and must be reinvested or remitted in accordance with his instructions or in accordance with the trust agreement. (R. 5, 41) Neither the trustee nor the distributing companies can deviate from the instructions given or from the terms of the trust agreements.

9. If profits are realized from the sale of shares, they are realized because the certificates of the particular investors have been terminated and the profits belong to these investors and cannot be distributed generally to all investors as profits of the trust. (R. 7, 43)

10. Losses, likewise, are suffered by the individual investors and cannot be charged against the trust generally

and against the investors who do not participate in the losses.

11. The individual investors may at any time revoke the trust as far as his particular interest is concerned. Partial liquidation of the assets of a corporation are made to classes of stockholders and not to individual stockholders.

12. The investors as a group have no right to terminate the trusts as a whole equivalent to the power of the stockholders of a corporation to dissolve it.

13. These trusts have no minute book or seal, no officers, employees or separate business stationery.

IV. THE INVESTORS ARE NOT ASSOCIATES.

In the *Morrissey* case this Court aptly observed that the term "association" implies "associates" (p. 356). We know of only one case in which this point has been raised and it is significant that it was raised and decided in favor of the taxpayer in *Equitable Trust Company v. Magruder, supra,* which involved a periodic payment plan trust.

One of the unusual features of the trusts involved in these cases is that fundamentally there is a separate trust for each investor, because the trustee is required to note the exact number of shares held for each investor upon a separate account. Each investor from time to time has an equitable title to the shares noted in his account in the same manner that the customers of a stock broker have a traceable title to stock held by the broker in street name. *Gorman v. Littlefield,* 229 U. S. 19.

If we place ourselves in the shoes of an investor who subscribes for a plan and consider the certificate which he receives, we will note that he has no reason to believe that he is concerned with what any other investor may do or with what the trustee may do with any other investor's money. Any one investor is concerned only with what payments he has made, what deductions the trustee makes from

his payments, the number of shares which are purchased for him and what the trustee does with his distributions or dividends. If he has subscribed for a certificate with insurance benefits he is also concerned with whether the trustee maintains his insurance, and if he dies, only his estate or personal representative is concerned with whether or not the insurance is collected. If he desires to withdraw he is interested only in the exact number of shares which are held for him and not in the shares which are held for any other investor. The distributions or dividends on his shares belong to him and to no other investor. If he terminates his plan and orders his shares sold the proceeds of sales, and the resulting capital gain or loss is his and his alone.

The capital gains tax which was paid in the Capital case for the year 1937 demonstrates our point. In that year 258 investors severally instructed the trustee to sell their shares. The shares of a considerable number of investors were sold at a gain. The shares of a few more were sold at a loss. The entire proceeds of each sale were distributed to the particular investor in accordance with the trust agreement including the capital gain where gains were realized. The investors who did not terminate but permitted their trust shares to remain in the possession of the trustee were not concerned in the slightest with these sales, yet if the trust was properly classified as an association a capital gains tax was assessable against the trust as a whole and investors who had no concern whatsoever with the gains realized were charged with the tax.

Cases Relied Upon by the Circuit Court.

In addition to the decisions of this Court in the *Morrissey* case and its companion cases, which the Circuit Court falied to apply properly, it relied on three decisions in other circuits.

Fidelity-Bankers Trust Co. v. Helvering, 113 F. (2d) 14, is a case where a syndicate had been created in trust form

to take over certain real estate assets of a failing bank, and to manage these assets for the purpose of repaying contributions of subscribers to the trusts and of dividing the profits between the subscribers and the bank. The principal argument of the taxpayer was that the transaction was essentially a loan and the decision of the United States Court of Appeals for the District of Columbia to the contrary was obviously sound. The Court in that case did not fall into the same error as the Circuit Court in our cases. It recognized that the Revenue Acts only tax trusts which are doing business for profit and that the ultimate question is whether the trust performs some non-business functions or operates a business enterprise as a going concern (see pages 17-18 of opinion).

The trust in *Commissioner v. North American Bond Trust*, 122 F. (2d) 545, was an investment trust similar to fixed investment trust which was not in fact fixed. The sponsoring company not only had the right to eliminate undesirable investments as in the usual fixed investment trust, but as new units were created it could deposit bonds other than those underlying units already created. In this way it could take advantage of market conditions and could vary at will the interests of those who were already beneficiaries of the trust. The case is a close one. We believe it was erroneously decided, and that the dissenting opinion is sound law.

In *Hamilton Depositors Corporation v. Nicholas*, 111 F. (2d) 385, the opinion shows that the sponsoring company "had large supervisory and directory powers over the trustee directing the trustee in the management, investment, and handling of property" (p. 387) and that the trust contemplated that the stocks to be purchased were to be sold and reinvested from time to time and "that the income and *profit* from the operation of the trust will be distributed and paid to the beneficiaries" (p. 386). (Italics ours.)

Conclusion.

The effect of the decision of the Circuit Court is to impose double taxation upon the investors by a strained construction of the Revenue Acts beyond their literal and ordinary meaning. The purpose of the trusts in these cases is to hold and conserve the trust res and collect the income. There is no purpose to engage in a business enterprise. They are not business trusts. They bear practically no resemblance to corporations in form, substance or operation. The interests of the investors in the trust res are several and not joint or common. The investors are not associates, nor are the activities of the trustee in any sense joint enterprises or common enterprises. The powers of substitution are incidental powers, considerably more restricted than the investment powers of an ordinary trustee. The decision of the Circuit Court is erroneous and fails to follow the decisions of this Court and well reasoned decisions of other federal courts.

It is therefore respectfully submitted that writs of certiorari should issue in these cases.

Respectfully submitted,

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